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Mercantile Stores Company, Inc.

Annual Report

Twelve Months Ended

January 31st

1948

MERCANTILE STORES COMPANY, INC.

BOARD OF DIRECTORS

JOHN E. BIERWIRTH
LINDSAY BRADFORD
F. K. BRADLEY
ASHTON HAWKINS
HAROLD W. JOCKERS
F. G. KINGSLEY
FREDERICK H. MESERVE
MINOT K. MILLIKEN
ROGER MILLIKEN

OFFICERS

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HAROLD W. JOCKERS, *President*
F. K. BRADLEY, *Vice-President*
A. D. CHURBUCK, *Vice-President*
FREDERICK H. MESERVE, *Vice-President*
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ASHTON HAWKINS, *Secretary*
E. F. FLANIGAN, *Controller*

Stock Transfer Agent
THE NEW YORK TRUST COMPANY
New York

Registrar of Stock
CITY BANK FARMERS TRUST COMPANY
New York

Stores Owned by

MERCANTILE STORES COMPANY, INC.

Principal Stores

J. Bacon & Sons	Louisville, Ky.
The Castner-Knott Dry Goods Co.	Nashville, Tenn.
Duluth Glass Block Store Company	Duluth, Minn.
The Fair Store Company	Cincinnati, Ohio
Hennessy Company	Butte, Mont.
The Jones Store Co.	Kansas City, Mo.
The Joslin Dry Goods Company	Denver, Colo.
The Lazarus Store, Inc.	Wilkes Barre, Pa.
The Lion Dry Goods Company	Toledo, Ohio
The MacDougall & Southwick Company	Seattle, Wash.
The McAlpin Company	Cincinnati, Ohio
Montgomery Fair Co.	Montgomery, Ala.
The People's Store Company	Tacoma, Wash.
Root Dry Goods Company	Terre Haute, Ind.
Thomas C. Watkins, Limited	Hamilton, Ont., Can.
J. B. White & Co.	Augusta, Ga.
J. B. White & Co.	Greenville, S. C.

Other Stores

33 Junior Department Stores

67 Appliance Stores

●

Represented in the markets by

WM. T. KNOTT COMPANY, INC.

(A wholly owned subsidiary company)

128 W. 31st Street, New York, N. Y.

756 South Broadway, Los Angeles, Calif.

180 W. Adams Street, Chicago, Ill.

MERCANTILE STORES COMPANY, INC.

AND SUBSIDIARIES

100 West 10th Street,
Wilmington, Delaware,

April 16, 1948

To the Stockholders of
Mercantile Stores Company, Inc.:

The annual report of your Company for the year ended January 31, 1948, is presented herewith on behalf of the Board of Directors. The following paragraphs give information on the various phases of the business.

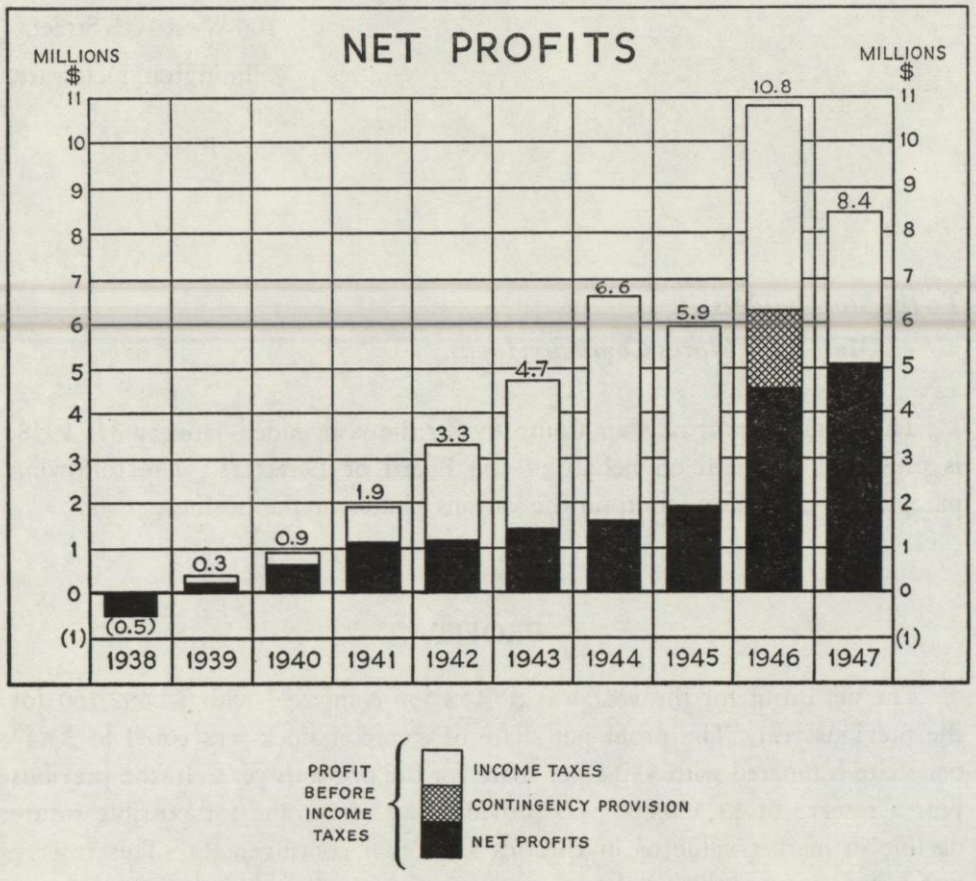
PROFIT

The net profit for the year was $5,158,538 compared with $4,682,760 for the previous year. The profit per share of common stock was equal to $3.47 per share compared with $3.14 per share for the previous year. In the previous year a reserve of $1,500,000 was provided out of income for possible future decline in market value of inventories and other contingencies. This reserve was left unchanged during the current year and is still included in the balance sheet of January 31, 1948.

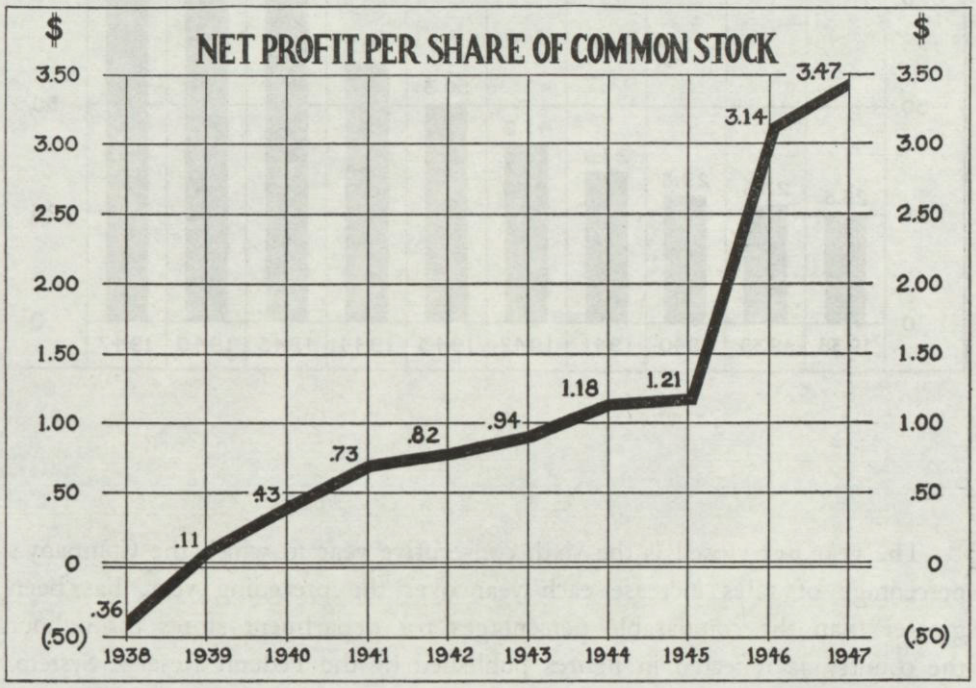
Earnings, before provision for taxes and for reserve for contingencies, amounted to $8,444,538 for the current year compared with $10,800,760 for the preceding year. Unusually large price reductions was the largest factor contributing to the decline in profit before taxes.

The expense ratio to sales did rise moderately during the current year, but the expense ratio is still a relatively low one.

The profit before income taxes and the final net profit for each of the last ten years are compared in the following chart.

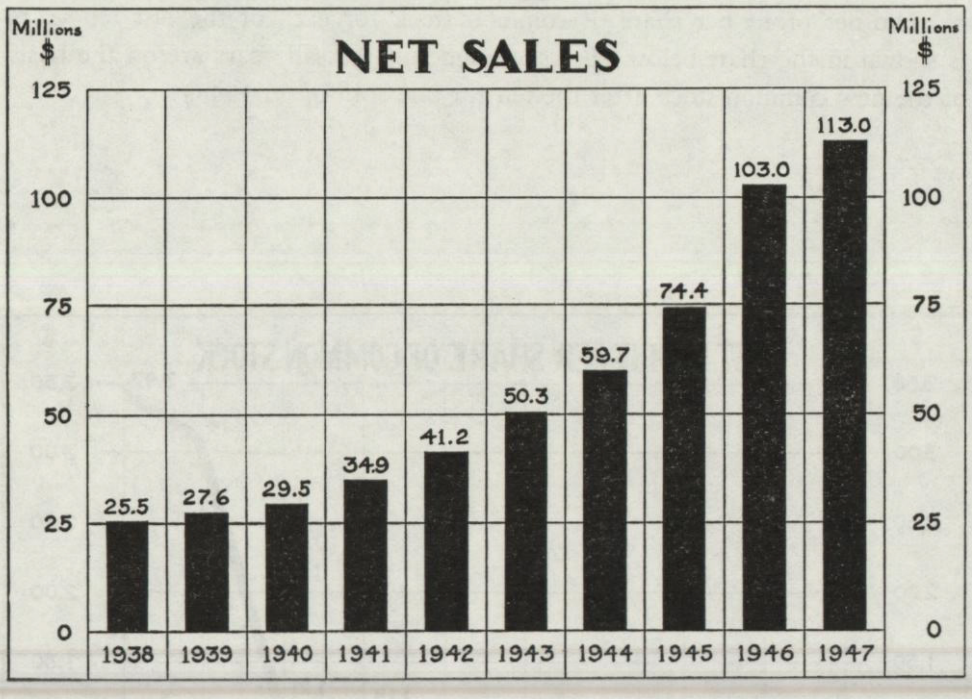


The net profit per share of common stock for each of the last ten years is shown in the chart below (per share amounts for all years are on the basis of the new common stock after the ten for one split-up in 1945).



SALES

Sales for the year amounted to $113,012,702 compared with $103,007,184 for the preceding year, an increase of 9.7%. The sales of the Company have shown a steady growth for the last ten years. The sales for the current year were more than double those of four years ago, and were more than four times those of ten years ago. The chart at the top of the next page shows the sales growth during the past ten years.



The year just closed is the sixth consecutive year in which the Company's percentage of sales increase each year over the preceding year, has been greater than the comparable percentages for department stores throughout the country as reflected in figures published by the Federal Reserve System.

Sales for February and March of 1948 were 7.1% ahead of the same period last year.

DIVIDENDS

The Company paid $1.00 per share in dividends on the common stock during the year ended January 31, 1948, which was the same amount as paid during the preceding year. The dividend of $1.00 per share might be considered to be low in comparison with the Company's earnings of the past few years. However, the retention of these earnings in the Company has made possible the considerable expansion of our operations which has been accomplished without

reducing the equity of the present stockholders by issuing additional stock. The amount of working capital in our Company during the past several years has been close to the minimum required to operate, but by careful husbanding of our financial resources we have grown substantially and have maintained a sound financial position.

The Company also paid during the current year the regular dividend on the preferred stock of which only 3,668 shares remain outstanding, exclusive of shares in the Company's treasury. The total dividends paid during the year just closed amounted to $25,676 on the preferred stock and $1,481,220 on the common stock. The earned surplus was increased during the year by $3,651,642.

INVENTORY

Total merchandise inventories at January 31, 1948 were slightly below those of a year ago. The inventories at the end of the current year amounted to $18,617,899 compared with $18,632,200 for the previous year. Inventory turnover for the year just closed was 5.6 times compared with 5.9 times for the previous year. The inventory contained only a negligible amount of old stock, and again the amount of merchandise on hand which was more than one year old was only a fraction of 1%. In our report a year ago, we stated that we thought the necessity for relatively large price reductions would continue for the greater part of the year, and that proved to be the case. Unusually large price reductions were taken during the Spring months and although the Fall months reflected an improvement in this phase of the operation, quite heavy reductions were still taken during the Fall season. Thus far, during the new fiscal year beginning February 1, 1948 price reductions have not been extreme, and the total for February and March is well below the amount for these months a year ago.

However, the future is difficult to predict and the management has thought it advisable to leave the inventory and contingency reserve of $1,500,000 intact and that reserve is available for future contingencies. It is uncertain what the general price structure will be during the coming months. As this report is written, the management does not foresee a repetition of the extreme markdowns which were required a year ago, but, of course, changes in market conditions which cannot be foreseen now might radically change that point of view.

SALES VOLUME OF OUR STORES

For the year just closed, the sales of our largest store amounted to over $16,000,000. The next nine large stores were in the $5,000,000 to $11,000,000 group and six of the major department stores were in the $2,000,000 to $5,000,000 classification, with one of the department store's volume being slightly under $2,000,000.

Sales of a majority of the junior stores ranged between $250,000 and $500,000 with one store above $1,100,000.

The average sales per store of the 67 small appliance stores were $93,100.

BASIC POLICIES

Your Company operates quite differently from the average or typical department store and the difference stems from several basic policies of the Company.

First, we believe in pricing our goods to meet the competition of the stores in our localities which sell at the lowest prices for comparable values. It is our experience that generally speaking, and with some exceptions, the chain stores are the businesses which do so sell at the lowest price in our communities. The result of following this low price policy is that the mark-up percentage for our Company (by mark-up percentage is meant the profit spread or difference between cost and the retail price put on goods for sale) is definitely lower than that of department stores in general as evidenced by mark-up figures published by such sources as Harvard University Graduate School of Business Administration and National Retail Dry Goods Association (NRDGA).

Selling goods at low prices cannot be continued profitably unless goods are bought as advantageously as is done by successful chain stores. This requires centralized buying and to a considerable extent, centralized merchandising and planning. Your Company has been perfecting for some years now the organization necessary to operate in this manner.

Finally, to compete in prices with chain stores, and still operate profitably, operating expenses must be kept lower than those of the average department store. The expense ratio to sales of your Company has been definitely lower than that of the average department store (again referring to published figures from generally recognized sources).

These three basic principles of low prices, centralized buying and low expense ratio are fundamental policies on which the management intends to build your Company in the future.

The management subscribes wholeheartedly to the general proposal frequently expressed that the cost of distribution must come down. We think that the policies of your Company make it possible for us to consistently offer merchandise of good quality to our customers at the lowest possible prices. In our opinion, this price policy over the years is the major reason for our sales increases continuing to be better than published figures for the industry.

EXPANSION

The Company continued its expansion policy in opening new stores. During the year 1947, seven junior department stores were opened as follows: in June, one in Jeffersonville, Indiana, and one in South Tacoma, Washington; in July a store in Carbondale, Pennsylvania; in August, a store in Port Angeles, Washington; in November, one in Brantford, Ontario, Canada, and one in Shamokin, Pennsylvania; and in December a store in Paris, Kentucky.

These new stores have increased the total annual volume of the Company by approximately $2,425,000 based upon current operations.

Our experience with the junior department stores as a group has definitely been favorable and our conclusion is that for the most part they will continue to be profitable stores.

The properties in which these junior stores are operated are leased for relatively short terms with options for renewal included in the leases, for the most part.

The management continues to believe the opening of additional junior department stores is a sound and profitable expansion program. The experience of another year of operating these junior stores confirms our earlier conclusion that additional small stores can be added with only a relatively small increase in general overhead expense. Two new locations are under lease as this report is written but preparations for opening will not be completed for a number of months.

Four new small stores selling household appliances were opened during the year, which increased the number of such stores in operation to 67 at the end of the year.

At the end of the current year, your Company was operating seventeen major department stores, thirty-three junior department stores, and sixty-seven small stores selling household appliances.

During the year, your Company borrowed two million dollars from banks on a short term basis. These loans were all repaid before January 31, 1948, so the expansion was accomplished without additional borrowing existing at the end of the year.

IMPROVEMENTS TO PHYSICAL PROPERTIES

During the year $1,999,730 was spent by the Company for new fixtures and building improvements. Depreciation for the year amounted to $995,625, so the Company spent a little over a million dollars more than the amount of depreciation charged to earnings in making these improvements. Of the total spent, $537,876 was on junior store properties and the balance of $1,461,854 on the seventeen major department stores and appliance stores (principally on the department stores). In addition, the Company spent $774,734 for repairs to its properties of which $51,265 was for junior department stores. The management believes the properties have been maintained in a good state of repair and that the new fixtures and improvements have enabled our stores to keep abreast of our competitors in the various localities. It has been our policy to spend money to maintain clean, well lighted stores with attractive fixtures to display our merchandise, but to avoid extravagant expenditures for fixtures or building improvements.

In December, 1947, the Company and its Canadian subsidiary completed arrangements to purchase the store property in Hamilton, Ontario, Canada, on which the lease expires in October, 1948. The purchase price was $862,000. Under the purchase agreement, $50,000 was paid in December, 1947, $212,000 is to be paid in October, 1948, and the balance of $600,000 is to be secured by a mortgage running for ten years with privilege of paying off the debt at earlier dates. A loan in Canadian funds of $300,000 is currently being negotiated with an insurance company in connection with this purchase.

Various foreign exchange problems stood in the way of financing this purchase out of United States funds. The Hamilton store has been one of our more profitable stores for a number of years and the management considers this a very satisfactory purchase. The interest on the borrowings will be less than the rentals we have been paying under the lease arrangement.

PROFIT SHARING PLAN

The Profit Sharing Plan of the Company (which is entirely separate from the Pension Plan) has now been operating for seven years with the basic features of the plan unchanged during that time. It continues to work well in the opinion of the management, and is a real factor in the continuing progress of the Company.

The plan includes executives but extends well down into the organization so that approximately one-fifth of all our people participate in this particular plan. In addition, the sales-people in our stores are on an incentive plan under which they earn more if they sell more. Thus a large proportion of all our employees have a direct incentive to handle their jobs so that more profit is made by the Company.

Under the Profit Sharing Plan first referred to above, payments amounting to $1,736,900 were made to 1067 people for the current year. For the previous year the amount was $2,002,290 paid to 981 people.

PENSION PLAN

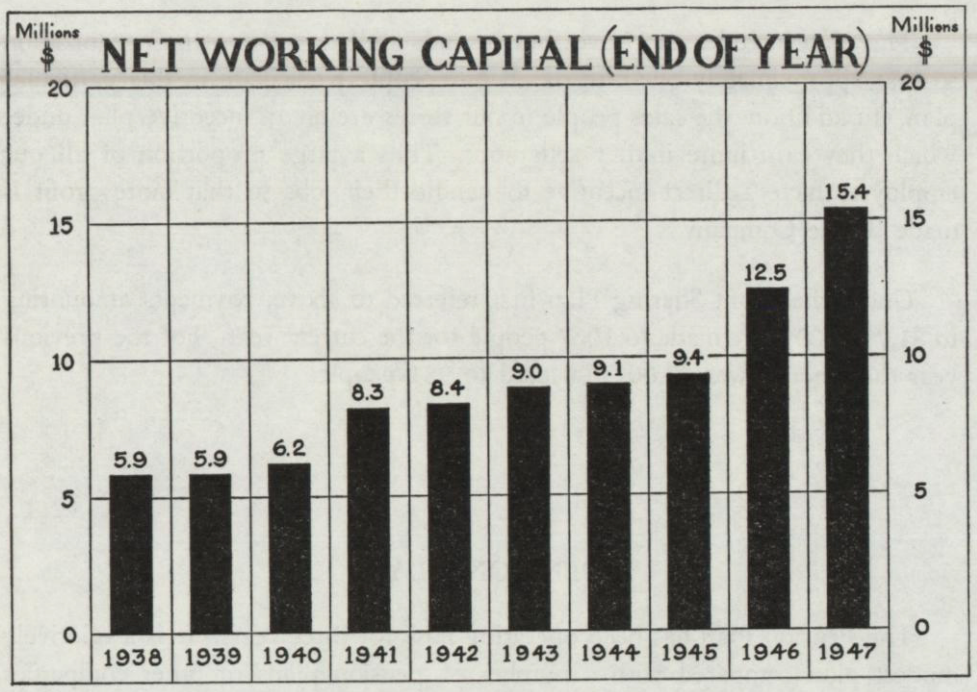
The Pension Plan has been operating now for three years. It is a relatively modest plan compared with a number of pension plans of other companies which have been reviewed by the management. There are now 350 employees included in the Plan. The Company's contribution to the Plan for the year just closed was $193,842 which amount has been paid over to the Trustee. The Company's contribution for the previous year was $146,640. The increase was not due to any change in the Plan — as there was no change — but rather

to the increase in earnings of our employees which resulted in making more people eligible to join the Plan and increasing the amounts for those who were previously participating.

The amount held by the Trustee in the fund at the end of the current year (including the contribution for the current year) was $442,521.

VARIOUS

The ratio of current assets to current liabilities was 2.2 to 1 at January 31, 1948, compared with 1.9 to 1 for the preceding year. The working capital at the end of each year for the past ten years is shown in the chart below:



The amount of earned surplus was increased during the year from $8,659,080 to $12,310,722.

The amount of customers' receivables as reflected in the balance sheet at January 31, 1948, was $6,481,865, an increase of $2,098,007 over the $4,383,858 total a year ago. This increase would have been larger except that the Company sells its installment contracts to a bank under an arrangement which has been operating satisfactorily for a number of years. The reserve for doubtful accounts was increased from $773,130 a year ago to $902,196 at January 31, 1948. The reserve is a generous one in the opinion of the management and the receivables are considered to be in a satisfactory condition.

At the end of the year our common stockholders numbered approximately 2600 compared with 2800 a year ago.

The report of our Auditors is given on the succeeding pages, and following that is a ten year comparison of sales, earnings, and surplus, together with a ten year comparison of Balance Sheets.

The management desires to express its appreciation for the continued loyalty and cooperation of the Company's employees.

Respectfully submitted,

F. G. KINGSLEY,

Chairman of the Board.

MERCANTILE STO

(a Delaware

AND SUBSIDIARY

CONSOLIDATED BALANCE

ASSETS

Current Assets:		
Cash		$ 3,349,732
Accounts receivable—		
Customers—		
Regular retail terms	$4,991,989	
Installment terms, including installments maturing after one year	1,064,921	
Equity in installment accounts sold (the uncollected balances of accounts sold amounted to $4,249,550)	424,955	
Due from suppliers, etc.	685,246	
	$7,167,111	
Less—Reserve for doubtful accounts	902,196	6,264,915
Merchandise inventories, priced at the lower of cost or market, as determined by the retail inventory method, except for merchandise in transit which is priced at cost		18,617,899
TOTAL CURRENT ASSETS		$28,232,546
Unexpired Insurance Premiums, Prepaid Rent, Etc.		468,939
Other Assets:		
U. S. Government securities deposited in escrow as guarantees of performance under leases, at cost	$ 178,643	
Post-war refund of Canadian excess profits taxes	88,000	
Other, including $50,000 deposit for purchase of real estate	62,865	329,508
Fixed Assets:		
Land and buildings owned, buildings on leased ground and leaseholds, and building improvements (property of a net book value of $225,502 is pledged to secure performance under a lease), at cost, less reserve for depreciation of $3,685,111	$5,166,861	
Store fixtures, etc., at cost, less reserve for depreciation of $1,949,656	4,781,308	9,948,169
		$38,979,162

RES COMPANY, INC.

corporation)

COMPANIES

SHEET – JANUARY 31, 1948

LIABILITIES

Current Liabilities:			
Accounts payable			$ 5,913,538
Accrued taxes (other than Federal income), salaries, rent, etc.			2,979,030
Reserve for Federal income taxes			3,812,766
Notes payable to banks including current maturities of mortgage notes			85,000
TOTAL CURRENT LIABILITIES			$12,790,334
Mortgage Notes Payable to Banks, due $5,000 semiannually until June 30, 1953 when remaining balance becomes due (less current maturities included above)			95,000
Deferred Carrying Charges on Installment Accounts			227,532
Reserve for Possible Future Decline in Market Value of Inventories and Other Contingencies			1,500,000
Capital Stock and Surplus:			
Capital stock—			
Preferred stock, 7% cumulative, $100 par value, callable at $105 per share—			
Authorized and issued, 10,410 shares	$1,041,000		
Less—Held in treasury, 6,742 shares (cost, $618,217)	674,200		
Outstanding, 3,668 shares		$ 366,800	
Common stock, par value $3.66⅔ per share—			
Authorized and issued, 1,582,380 shares	$5,802,060		
Less—Held in treasury, 101,160 shares (cost, $200,414)	370,920		
Outstanding 1,481,220 shares		5,431,140	
Surplus prior to February 1, 1935 (no change during year)		6,257,634	
Earned surplus since February 1, 1935		12,310,722	
(Surplus of $818,631 is restricted by reason of purchase of treasury stock until such stock is sold or canceled)			24,366,296
			$38,979,162

MERCANTILE STORES COMPANY, INC.

AND SUBSIDIARY COMPANIES

STATEMENTS OF CONSOLIDATED PROFIT AND LOSS AND EARNED SURPLUS

For the Year Ended January 31, 1948

PROFIT AND LOSS

Net sales, including sales of leased departments		$113,012,702
Cost of goods sold, selling, operating and administrative expenses, including depreciation of $995,625		105,006,904
Operating profit		$ 8,005,798
Other income (net):		
Carrying charges on installment accounts, miscellaneous income, etc. (net)	$ 519,364	
Less—Interest expense	80,624	438,740
Profit before provision for income taxes		$ 8,444,538
Provision for income taxes:		
Federal income tax	$2,990,000	
State and Canadian taxes	296,000	3,286,000
Net profit for the year		$ 5,158,538

EARNED SURPLUS SINCE FEBRUARY 1, 1935

Balance, January 31, 1947		$ 8,659,080
Net profit for the year ended January 31, 1948		5,158,538
		$ 13,817,618
Dividends declared:		
Preferred stock—$7.00 per share	$ 25,676	
Common stock—$1.00 per share	1,481,220	1,506,896
Balance, January 31, 1948		$ 12,310,722

AUDITORS' REPORT

To the Board of Directors,
Mercantile Stores Company, Inc.:

We have examined the consolidated balance sheet of Mercantile Stores Company, Inc. (a Delaware corporation) and subsidiary companies as at January 31, 1948, and the statements of consolidated profit and loss and earned surplus for the year ended that date. In connection therewith, we have reviewed the system of internal control and the accounting procedures of the companies and, without making a detailed audit of the transactions, have examined or tested accounting records of the companies and other supporting evidence, by methods and to the extent we deemed appropriate. Our examination was made in accordance with generally accepted auditing standards applicable in the circumstances and included all procedures which we considered necessary.

In our opinion, the accompanying consolidated balance sheet and related statements of consolidated profit and loss and earned surplus present fairly the position of the companies at January 31, 1948, and the results of their operations for the year ended that date and are in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Arthur Andersen & Co.

New York, N. Y.,
April 12, 1948.

MERCANTILE STO

AND SUBSIDIARY

TEN YEAR COMPARISON OF SALES,

Fiscal Year Ended January 31	Net Sales	Profit Before Income Taxes	Income Taxes	Net Profit
1948	$113,012,702	$ 8,444,538	$3,286,000	$5,158,538
1947	103,007,184	10,800,760	4,618,000	4,682,760**
1946	74,407,149	5,894,901	4,084,000	1,810,901
1945	59,668,304	6,633,941	4,854,000	1,779,941
1944	50,277,807	4,700,875	3,276,760	1,424,115
1943	41,173,113	3,340,264	2,118,645	1,221,619
1942	34,867,853	1,912,941	812,164	1,100,776
1941	29,509,394	939,991	278,547	661,443
1940	27,619,565	274,646	72,059	202,586
1939	25,467,539	*486,264**	3,850	*490,114**

* Italics indicate loss or deficit.

** After deducting special provision of $1,500,000 for possible future decline in market

*** Principally dividends on common stock, annual dividends on preferred stock ranged from

RES COMPANY, INC.

COMPANIES

EARNINGS AND EARNED SURPLUS

Net Profit Per Common Share (After 10 for 1 Splitup in 1945)	Dividends Paid***	Earned Surplus (End of Year)	Book Value Per Common Share (After 10 for 1 Splitup in 1945)
$3.47	$1,506,896	$12,310,722	$16.19
3.14	1,506,896	8,659,080	13.72
1.21	395,981	5,483,216	11.58
1.18	398,756	4,068,296	10.63
.94	405,106	2,687,111	9.69
.82	398,388	1,668,102	9.20
.73	330,631	844,871	8.58
.43	331,344	74,726	8.07
.11	42,504	*255,372**	7.85
*.36**	46,907	*415,455**	7.59

value of inventories and other contingencies.

$46,907 in earliest year to $25,676 in past two years.

MERCANTILE STO

AND SUBSIDIARY

TEN YEAR COMPARISON

	January 31,			
ASSETS	*1948*	*1947*	*1946*	*1945*
Cash	$ 3,349,732	$ 2,668,226	$ 3,058,809	$ 3,542,395
Receivables, less Reserves	6,264,915	4,629,841	2,973,050	2,559,611
Merchandise Inventories	18,617,899	18,632,200	11,116,080	7,817,194
TOTAL CURRENT ASSETS	$28,232,546	$25,930,267	$17,147,939	$13,919,200
Prepaid Expenses	468,939	679,625	692,000	409,297
Other Assets	329,508	268,621	280,826	624,429
Fixed Assets (Net)	9,948,169	8,944,064	7,361,003	6,298,478
	$38,979,162	$35,822,577	$25,481,768	$21,251,404
LIABILITIES				
Current Liabilities	$12,790,334	$13,404,957	$ 7,724,450	$ 4,866,107
Long Term Debt	95,000	105,000	115,000	125,000
Reserves and Deferred Income	1,727,532	1,597,966	103,528	135,439
Capital Stock	5,797,940	5,797,940	5,797,940	5,798,928
Surplus*	18,568,356	14,916,714	11,740,850	10,325,930
	$38,979,162	$35,822,577	$25,481,768	$21,251,404
Net Working Capital	$15,442,212	$12,525,310	$ 9,423,489	$ 9,053,093

* Includes surplus prior to February 1, 1935 of $6,257,634, unchanged during ten year period.

RES COMPANY, INC.

COMPANIES

OF BALANCE SHEETS

		January 31,			
1944	*1943*	*1942*	*1941*	*1940*	*1939*
$ 3,652,070	$ 2,551,575	$ 2,764,570	$ 1,582,371	$ 1,530,289	$ 1,595,295
2,369,795	2,781,126	4,319,635	3,605,464	3,440,468	3,313,964
6,956,591	6,623,978	4,340,148	2,922,536	2,807,643	2,961,153
$12,978,456	$11,956,679	$11,424,353	$ 8,110,371	$ 7,778,400	$ 7,870,412
399,839	408,734	531,841	181,153	251,848	227,771
529,752	276,726	119,190	157,931	156,429	158,873
5,944,141	6,125,551	6,098,917	6,037,061	5,857,639	5,921,452
$19,852,188	$18,767,690	$18,174,301	$14,486,516	$14,044,316	$14,178,508
$ 3,963,093	$ 3,514,212	$ 3,169,427	$ 1,951,782	$ 1,916,609	$ 1,978,857
800,000	1,200,000	1,600,000	—	—	96,733
187,922	247,391	342,799	241,416	150,000	165,000
5,956,428	5,880,351	5,959,570	5,960,958	5,975,446	6,095,740
8,944,745	7,925,736	7,102,505	6,332,360	6,002,261	5,842,178
$19,852,188	$18,767,690	$18,174,301	$14,486,516	$14,044,316	$14,178,508
$ 9,015,363	$ 8,442,467	$ 8,254,926	$ 6,158,589	$ 5,861,791	$ 5,891,555